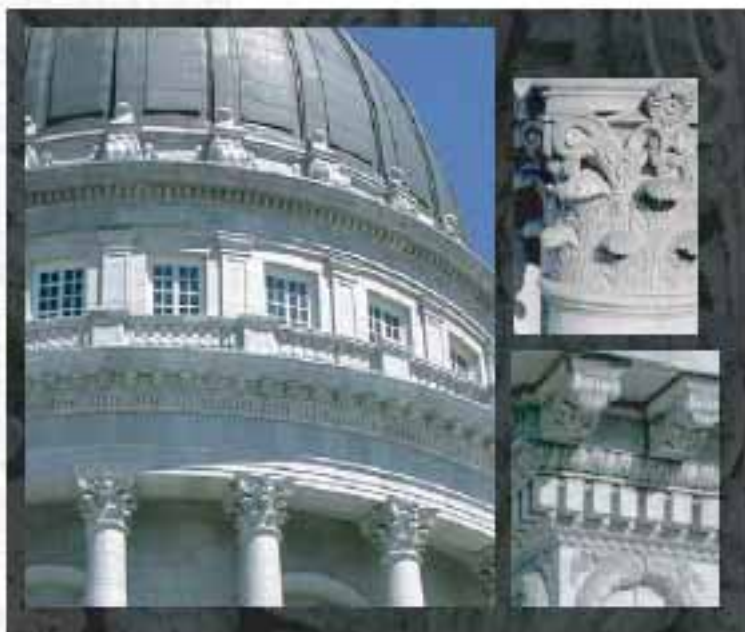


STATE OF UTAH

Comprehensive Annual Financial Report



'07

For the Fiscal Year Ended JUNE 30, 2007

State Of Utah
COMPREHENSIVE ANNUAL FINANCIAL REPORT
For The Fiscal Year Ended June 30, 2007

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Gary R. Herbert Lt. Governor
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Special appreciation is given to all of the budget and accounting officers throughout the State whose extra time and effort made this report possible.



Department of Administrative Services: Division of Finance Accounting Standards and Financial Reporting Section

State of Utah
COMPREHENSIVE ANNUAL FINANCIAL REPORT

For the Fiscal Year Ended June 30, 2007

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State of Utah
COMPREHENSIVE ANNUAL FINANCIAL REPORT

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INTRODUCTION

The following is a discussion and analysis of the State of Utah's financial performance and position, providing an overview of the State's activities for the fiscal year ended June 30, 2007. Please read it in conjunction with the transmittal letter in the Introductory Section of this report and with the State's financial statements that follow this section.

HIGHLIGHTS

Government-wide

- The State's total net assets increased \$1.972 billion or 14.1 percent over the prior year. Net assets of governmental activities increased \$1.718 billion or 14.4 percent due to a strong economy and active resource management. Net assets of business-type activities also grew significantly, increasing by \$254.3 million or 12.3 percent, primarily due to revenues from employers' unemployment premiums exceeding benefit payments for the third consecutive year.

Fund Level

- Combined tax revenues were 2.1 percent higher in the General Fund and 11 percent higher in the Education Fund than the prior year. Overall, sales tax revenues grew by 10.6 percent. However, the Legislature reduced the sales tax rate on unprepared food by 2 percent and diverted additional sales tax revenues to fund highway projects. Thus, sales tax revenue in the General Fund grew by only 2.2 percent. The State's economic slowdown in fiscal years 2002 and 2003 and subsequent improvement in fiscal years 2004 through 2006 was similar to the trend of the national economy. However, in fiscal year 2007, Utah's economic expansion was above that of the national economy.
- The General Fund and Uniform School Fund ended the fiscal year with "surplus" from unreserved and undesignated sources of \$64.8 million and \$176.9 million, respectively. Balances in the General Fund Budget Reserve Account ("Rainy Day Fund") and the Education Budget Reserve Account are at an all time high of \$170.6 million and \$142.8 million respectively, as a result of appropriations to these funds authorized by the Legislature. In addition, by law, \$22.1 million of the surplus in the General Fund was transferred to the newly created Disaster Recovery Restricted Account.

Long-term Debt

- The State's long-term bonded debt decreased a net \$174.6 million or 4.5 percent through payment of principal balances on outstanding debt. No new general obligation bonds or revenue bonds were issued.

OVERVIEW OF THE FINANCIAL STATEMENTS

This report includes the State's Basic Financial Statements, Required Supplementary Information, and Supplementary Information. The Basic Financial Statements include three components: government-wide financial statements, fund financial statements, and notes to the financial statements.

Government-wide Statements – Reporting the State as a Whole

The Statement of Net Assets and the Statement of Activities beginning on page 27 together comprise the *government-wide financial statements*. These statements provide a broad overview of the State's finances as a whole with a long-term focus and are prepared using the *full-accrual* basis of accounting, similar to private-sector companies. This means all revenues and expenses are recognized regardless of when cash is received or spent, and all assets and liabilities, including capital assets and long-term debt, are reported at the entity level.

The government-wide statements report the State's *net assets* – the difference between total assets and total liabilities – and how they have changed from the prior year. Over time, increases and decreases in net assets measure whether the State's overall financial condition is getting better or worse. In evaluating the State's overall condition, however, additional non-financial factors should be considered such as the State's economic outlook, changes in its demographics, and the condition of its capital assets and infrastructure. The government-wide statements report three activities:

Governmental Activities – Most of the State's basic services fall under this activity including education, transportation, public safety, courts, corrections, health, and human services. Taxes and federal grants are the major funding sources for these programs.

Business-type Activities – The State operates certain activities much like private-sector companies by charging fees to customers to cover all or most of the costs of providing the goods and services. Student loans, unemployment compensation, water project loan programs, and liquor sales are examples of business-type activities.

Component Units – A number of entities are legally separate from the State, yet the State remains financially accountable for them. Colleges and Universities, Utah Housing Corporation, and Utah State Fair Corporation are examples of component units.

Fund Financial Statements – Reporting the State's Most Significant Funds

The fund financial statements beginning on page 32 provide detailed information about individual major funds, not the State as a whole. A fund is a group of related accounts that the State uses to keep track of specific resources that are segregated for a specific purpose. Some funds are required by law to exist, while others are established internally to maintain control over a particular activity. All of the State's funds are divided into three types, each of which uses a different accounting approach.

Governmental Funds – Most of the State's basic services are accounted for in governmental funds and are essentially the same functions reported as *governmental activities* in the government-wide statements. Governmental funds use the *modified accrual* basis of accounting, which measures the flow of current financial resources that can be converted to cash and the balances left at yearend that are available for future spending. This *short-term* view of the State's financial position helps determine whether the State has sufficient resources to cover expenditures for its basic services in the near future.

Proprietary Funds – Proprietary funds include enterprise funds and internal service funds and account for state activities that are operated much like private-sector companies. Like the government-wide statements, proprietary fund statements are presented using the *full-accrual* basis of accounting. Activities whose customers are mostly outside of state government (e.g., water project loans to local governments) are accounted for in *enterprise funds* and are the same functions reported as *business-type activities*. Thus, the *enterprise fund* financial statements reinforce the information reported for *business-type* activities in the government-wide statements, but provide more detail and additional information, such as cash flows. Activities whose customers are mostly other state agencies (e.g., motor pool) are accounted for in *internal service funds*. The internal service fund activities are consolidated with the governmental activities in the government-wide statements because those services predominantly benefit governmental rather than business-type activities.

Fiduciary Funds – Fiduciary funds account for assets that, because of trust relationships, can be used only for trust beneficiaries. The State is responsible for ensuring these assets are used for their intended purposes. Fiduciary funds use *full-accrual* accounting, but are *not* included in the government-wide statements because their assets are not available to finance the State's own programs.

Reconciliation between Government-wide and Fund Statements

The financial statements include schedules on pages 34 and 38 that reconcile and explain the differences between the amounts reported for *governmental activities* on the government-wide statements (full-accrual accounting, long-term focus) with amounts reported on the *governmental* fund statements (modified accrual accounting, short-term focus). The following are some of the major differences between the two statements:

- Capital assets and long-term debt are included on the government-wide statements, but are not reported on the governmental fund statements.
- Capital outlay spending results in capital assets on the government-wide statements, but are expenditures on the governmental fund statements.
- Bond proceeds result in liabilities on the government-wide statements, but are other financing sources on the governmental fund statements.
- Certain tax revenues that are earned but not yet available are reported as revenue on the government-wide statements, but are deferred revenue on the governmental fund statements.

Notes to the Financial Statements

The notes beginning on page 58 provide additional schedules and information that are essential to a complete understanding of the financial statements. The notes apply to both the government-wide financial statements and the fund financial statements.

Required Supplementary Information (RSI)

Following the Basic Financial Statements are budgetary comparison schedules for major funds with legally adopted budgets and condition assessment data related to infrastructure. In addition, the RSI includes schedules on the funded status and employer contributions for the State's defined benefit Other Postemployment Benefit Plan. RSI further supports the information in the basic financial statements.

Supplementary Information

Supplementary Information includes combining statements for the State's nonmajor governmental, nonmajor proprietary and fiduciary funds and for nonmajor discretely presented component units. This section also includes schedules which compare budgeted expenditures to actual results at the legal level of control, which is generally the line item level of the *Appropriation Acts*.

FINANCIAL ANALYSIS OF THE STATE AS A WHOLE

Net Assets

The State's total net assets increased \$1.972 billion or 14.1 percent in fiscal year 2007. In comparison, net assets in the prior year increased \$1.864 billion or 15.3 percent. This increase in net assets resulted from a strong economy and the active management of state resources. Approximately \$726.9 million of the increase was in net capital assets as the State's investment in highways and buildings exceeded depreciation and no additional debt was used to finance projects. Total restricted net assets increased \$859.4 million or 24.4 percent over the prior year. The \$664.3 million increase in restricted net assets of governmental activities was primarily due to an increase of \$351.6 million in expendable net assets for public education as a result of increased individual income and corporate tax revenues. Also, nonexpendable net assets for public education increased \$232.9 million as a result of an increase in net earnings in the permanent Trust Lands Fund. Restricted net assets in business-type activities increased \$195 million primarily due to unemployment compensation revenues exceeding related claims by \$150.9 million. The increase of \$307.3 million in unrestricted net assets of governmental activities was primarily due to an increase in the unrestricted carry-forward balances in the General Fund and other governmental funds of \$190.6 million and \$110.6 million, respectively. The increase of \$78.3 million in unrestricted net assets of business-type activities was the result of normal operations and is primarily due to the State providing additional capital to the loan funds from mineral lease revenues and sales taxes. Net assets of business-type activities generally can be used only to finance the on-going operations of business-type activities.

State of Utah
Net Assets as of June 30
(Expressed in Thousands)

	Governmental Activities		Business-type Activities		Total Primary Government	
	2007	2006	2007	2006	2007	2006
Current and Other Assets	\$ 5,450,206	\$ 4,356,335	\$ 4,564,541	\$ 4,294,237	\$ 10,014,747	\$ 8,650,572
Capital Assets	10,878,861	10,247,267	52,462	66,974	10,931,323	10,314,241
Total Assets	16,329,067	14,603,602	4,617,003	4,361,211	20,946,070	18,964,813
Current and Other Liabilities	841,033	692,891	45,937	47,057	886,970	739,948
Long-term Liabilities	1,815,220	1,955,484	2,251,886	2,249,277	4,067,106	4,204,761
Total Liabilities	2,656,253	2,648,375	2,297,823	2,296,334	4,954,076	4,944,709
Net Assets:						
Invested in Capital Assets,						
Net of Related Debt	9,465,667	8,719,751	13,008	32,068	9,478,675	8,751,819
Restricted	3,043,599	2,379,269	1,334,737	1,139,691	4,378,336	3,518,960
Unrestricted	1,163,548	856,207	971,435	893,118	2,134,983	1,749,325
Total Net Assets	\$ 13,672,814	\$ 11,955,227	\$ 2,319,180	\$ 2,064,877	\$ 15,991,994	\$ 14,020,104
Percent change in total net assets from prior year	14.4 %		12.3 %		14.1 %	

The largest component of the State's net assets, 59.3 percent, reflects investments in capital assets (e.g., land, buildings, equipment, roads, and other infrastructure) less the outstanding debt issued to finance those assets. As capital assets, these resources are not available for future spending, nor can they be readily liquidated to pay off their related liabilities. Resources needed to repay capital-related debt must be provided from other sources.

Restricted net assets comprise 27.4 percent of total net assets and are subject to constitutional, legal, or external constraints on how they can be used. Net assets that are restricted by the *Constitution of Utah* include income and corporate taxes that can be used only for public and higher education costs and motor fuel taxes that can be used only for transportation expenses.

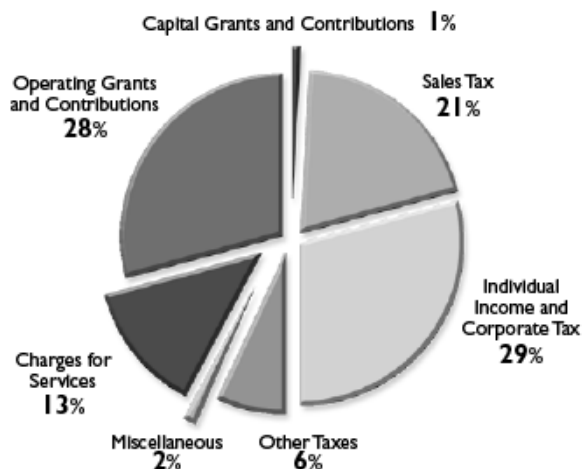
The remaining balance of unrestricted net assets may be used to meet the State's ongoing obligations, though certain laws and internally imposed designations of resources further limit the purposes for which many of those net assets may be used.

The following schedule and charts summarize the State's total revenues, expenses, and changes in net assets for fiscal year 2007.

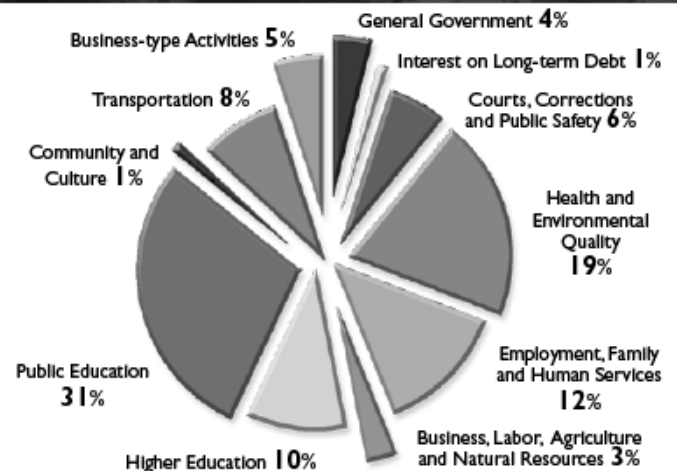
State of Utah
Changes in Net Assets
for the Fiscal Year Ended June 30
(Expressed in Thousands)

	Governmental Activities		Business-type Activities		Total Primary Government		Total Percentage Change
	2007	2006	2007	2006	2007	2006	2006 to 2007
Revenues							
General Revenues:							
Taxes	\$ 5,885,196	\$ 5,470,916	\$ 25,440	\$ 14,875	\$ 5,910,636	\$ 5,485,791	7.7 %
Other General Revenues	179,503	124,939	877	308	180,380	125,247	44.0 %
Program Revenues:							
Charges for Services	732,481	705,095	597,727	589,104	1,330,208	1,294,199	2.8 %
Operating Grants and Contributions	2,769,644	2,744,231	138,252	109,140	2,907,896	2,853,371	1.9 %
Capital Grants and Contributions	122,939	100,519	—	—	122,939	100,519	22.3 %
Total Revenues	9,689,763	9,145,700	762,296	713,427	10,452,059	9,859,127	6.0 %
Expenses							
General Government	328,779	289,749	—	—	328,779	289,749	13.5 %
Human Services and Youth Corrections	634,265	595,337	—	—	634,265	595,337	6.5 %
Corrections, Adult	237,305	208,922	—	—	237,305	208,922	13.6 %
Public Safety	172,912	182,042	—	—	172,912	182,042	(5.0)%
Courts	115,811	109,180	—	—	115,811	109,180	6.1 %
Health and Environmental Quality	1,620,936	1,635,544	—	—	1,620,936	1,635,544	(0.9)%
Higher Education	824,503	810,228	—	—	824,503	810,228	1.8 %
Employment and Family Services	393,938	405,845	—	—	393,938	405,845	(2.9)%
Natural Resources	174,711	133,441	—	—	174,711	133,441	30.9 %
Community and Culture	108,110	84,843	—	—	108,110	84,843	27.4 %
Business, Labor, and Agriculture	92,441	90,573	—	—	92,441	90,573	2.1 %
Public Education	2,548,391	2,321,139	—	—	2,548,391	2,321,139	9.8 %
Transportation	702,833	640,251	—	—	702,833	640,251	9.8 %
Interest on Long-term Debt	64,019	70,345	—	—	64,019	70,345	(9.0)%
Student Assistance Programs	—	—	174,220	152,895	174,220	152,895	13.9 %
Unemployment Compensation	—	—	97,692	102,476	97,692	102,476	(4.7)%
Water Loan Programs	—	—	13,042	6,560	13,042	6,560	98.8 %
Other Business-type Activities	—	—	176,261	155,265	176,261	155,265	13.5 %
Total Expenses	8,018,954	7,577,439	461,215	417,196	8,480,169	7,994,635	6.1 %
Excess Before Transfers	1,670,809	1,568,261	301,081	296,231	1,971,890	1,864,492	
Transfers	46,778	(19,013)	(46,778)	19,013	—	—	
Change in Net Assets	1,717,587	1,549,248	254,303	315,244	1,971,890	1,864,492	
Net Assets – Beginning as Adjusted	11,955,227	10,405,979	2,064,877	1,749,633	14,020,104	12,155,612	
Net Assets – Ending	\$ 13,672,814	\$ 11,955,227	\$ 2,319,180	\$ 2,064,877	\$ 15,991,994	\$ 14,020,104	14.1 %

STATE OF UTAH TOTAL REVENUES - FY 2007



STATE OF UTAH TOTAL EXPENSES - FY 2007



Changes in Net Assets

This year the State received 56.5 percent of its revenues from state taxes and 29 percent of its revenues from grants and contributions, mostly from federal sources. In the prior year, state taxes accounted for 55.6 percent and grants and contributions were 30 percent of total revenues. Charges for goods and services such as licenses, permits, liquor sales, park fees, and court fees, combined with other miscellaneous collections, comprised 14.5 percent of total revenues in fiscal year 2007, compared to 14.4 percent in fiscal year 2006.

Governmental Activities

The State's total governmental revenues from all sources increased \$544.1 million or 6 percent. Tax revenues increased \$414.3 million or 7.6 percent. This increase in taxes reflects strong economic conditions and is similar to the increase at the fund level. However, due to differences in measurement focus and timing of collections, the increase at the government-wide level should not be used to predict future increases at the fund statement or budget level. Other significant changes in governmental activities' revenues and expenses mirror the changes in the General Fund at the fund level. For further discussion of these changes, see the section entitled "General Fund" on page 19.

The following table shows to what extent the State's governmental activities relied on taxes and other general revenues to cover all of their costs. For fiscal year 2007, state taxes and other general revenues covered 54.8 percent of expenses. The remaining \$3.625 billion or 45.2 percent of the total expenses were covered by charges for services and grants. Although federal mineral lease revenue decreased \$10.9 million from a record high in fiscal year 2006, it was still the largest single factor that caused program revenues to exceed program expenses by \$20.1 million in the general government function.

State of Utah
Net Cost of Governmental Activities
for the Fiscal Year Ended June 30
(Expressed in Thousands)

	Program Expenses 2007	Less Program Revenues 2007	Net Program Costs		Program Revenues as a Percentage of Program Expenses	
			2007	2006	2007	2006
General Government	\$ 328,779	\$ (348,851)	\$ (20,072)	\$ (41,766)	106.1 %	114.4 %
Human Services and Youth Corrections	634,265	(286,997)	347,268	308,743	45.2	48.1 %
Corrections, Adult	237,305	(4,634)	232,671	203,915	2.0	2.4 %
Public Safety	172,912	(101,120)	71,792	80,009	58.5	56.0 %
Courts	115,811	(46,815)	68,996	61,246	40.4	43.9 %
Health and Environmental Quality	1,620,936	(1,225,847)	395,089	369,979	75.6	77.4 %
Higher Education	824,503	(2,360)	822,143	808,692	0.3	0.2 %
Employment and Family Services	393,938	(330,415)	63,523	52,677	83.9	87.0 %
Natural Resources	174,711	(110,612)	64,099	47,404	63.3	64.5 %
Community and Culture	108,110	(44,095)	64,015	44,275	40.8	47.8 %
Business, Labor, and Agriculture	92,441	(74,522)	17,919	17,499	80.6	80.7 %
Public Education	2,548,391	(565,759)	1,982,632	1,814,182	22.2	21.8 %
Transportation	702,833	(483,037)	219,796	190,394	68.7	70.3 %
Interest on Long-term Debt	64,019	—	64,019	70,345		
Total Governmental Activities	\$ 8,018,954	\$ (3,625,064)	\$ 4,393,890	\$ 4,027,594	45.2 %	46.8 %

Business-type Activities

Revenues from the State's business-type activities increased \$48.9 million or 6.9 percent from the prior year. The increase is primarily due to a \$32.2 million increase in investment income, and a \$10.6 million increase in tax revenues in the Water Loan Programs. Total expenses for the State's business-type activities increased \$44 million, or 10.6 percent. The increase was largely due to interest expense increasing \$35.1 million in the Student Assistance Programs, as a result of rising bond interest rates and bond related fees.

All of the State's business-type activities operate from program revenues, except for the Water Loan Programs and the Agriculture Loan Fund that by law receive dedicated sales taxes and the Community Impact Loan Fund that receives federal mineral lease

revenues to provide additional capital for loans. Accounting standards require unemployment taxes that are collected from employers and deposited in the Unemployment Compensation Fund to be reported as charges for services rather than taxes. Therefore, taxes in the business-type activities are comprised entirely of sales taxes in the water and agriculture loan programs.

FINANCIAL ANALYSIS OF THE STATE'S GOVERNMENTAL FUNDS

Fund Balances

At June 30, 2007, the State's governmental funds reported combined ending fund balances of \$4.022 billion. Of this amount, \$1.97 billion or 49 percent is reserved for specific programs by state law, by external constraints, or by contractual obligations. Unspent bond proceeds, balances of restricted accounts, and agencies' nonlapsing balances are included in reserved fund balance. An additional \$1.629 billion or 40.5 percent of total fund balances has been designated through internally imposed limitations on uses of certain funds. Note 11 on page 97 provides more details about reserved and designated fund balances at June 30, 2007. The remaining \$422.4 million or 10.5 percent of fund balance is available for appropriation for the general purposes of the funds.

State of Utah Governmental Fund Balances as of June 30, 2007 (Expressed in Thousands)

	General Fund	Education Fund	Uniform School Fund	Transportation Fund	Transportation Investment Fund	Trust Lands Fund	Nonmajor Funds	Total
Reserved	\$ 411,600	\$ —	\$ 102,200	\$ 51,285	\$ 110,891	\$ 983,881	\$ 310,350	\$ 1,970,207
Unreserved Designated	603,165	566,672	372,577	49,787	18,917	—	17,801	1,628,919
Unreserved Undesignated	64,807	—	176,947	225,945	—	—	(45,045)	422,654
Total	\$ 1,079,572	\$ 566,672	\$ 651,724	\$ 327,017	\$ 129,808	\$ 983,881	\$ 283,106	\$ 4,021,780
Percent change from prior year ..	24.2 %	63.9 %	9.2 %	55.8 %	(10.0)%	31.0 %	10.3 %	26.7 %

General Fund

During fiscal year 2007, the General Fund's total fund balance increased \$210.4 million or 24.2 percent. This increase was due in large part to sales tax revenues coming in \$51.3 million greater than budgeted and to \$223.6 million being set aside in the budget and designated by the Legislature for fiscal year 2008 appropriations. In contrast, the Legislature designated \$155.5 million for fiscal year 2007 appropriations in the prior year.

The General Fund ended fiscal year 2007 with a "surplus" from unreserved and undesignated sources of \$88.4 million. State law normally requires 25 percent of the "surplus" to be transferred to the General Fund Budget Reserve Account ("Rainy Day Fund"). However, state law limits the combined totals of the General Fund Budget Reserve Account and Education Budget Reserve Account to 6 percent of combined appropriations from certain funds. At fiscal 2007 yearend, the combined totals exceeded the 6 percent limit. As a result, no surplus transfer was made to the General Fund Budget Reserve Account; however, the Legislature appropriated almost \$32 million in fiscal year 2007 to the account, resulting in an increase to designated fund balance. In addition, the Legislature created the Disaster Recovery Restricted Account, effective for fiscal year 2007, to fund state costs directly related to a declared disaster. According to state law, this fund receives 25 percent of the surplus in the General Fund after any surplus transfer to the General Fund Budget Reserve Account. As a result, \$22.1 million was transferred to the Disaster Recovery Restricted Account, increasing designated fund balance. An additional \$1.5 million was carried forward by law for other purposes as designated for specific appropriation in 2007. The General Fund ended the year with \$64.8 million in unreserved/undesignated fund balance. Miscellaneous changes resulting from other designated and reserved sources account for the remaining change in fund balance. The General Fund Budget Reserve Account ended fiscal year 2007 with a balance of \$170.6 million.

Total General Fund revenues increased \$53.4 million or 1.2 percent from the prior year. Total tax collections increased \$43.1 million or 2.1 percent. The major positive change in tax revenues was sales tax, which increased \$39.7 million or 2.2 percent, a result of Utah's continued strong economy. The growth in sales tax revenue would have been much higher except that the Legislature reduced the sales tax rate on unprepared food by 2 percent, effective January 1, 2007, and diverted additional sales tax revenue to fund transportation projects, as discussed in the section entitled "Transportation Investment Fund" on page 21. Investment income was the largest single factor in increasing non-tax revenues for the fiscal year, as investment income increased \$47.4 million or 100.8 percent due to a favorable interest rate environment the past year. Charges for services increased \$11.5 million or 4.5 percent, driven by demand for services. The increase in revenues were offset by a decrease in federal contracts and grants of \$41 million or 2.2 percent and a decrease in federal mineral lease revenues of \$10.9 million or 6.9 percent.

Total General Fund expenditures increased by \$164.2 million or 3.8 percent. The increase was due in part to a 3.5 percent cost-of-living adjustment provided for state employees, and a 2.3 percent increase for employee benefits. In addition, the General Fund expenditures increased in part due to funding of other postemployment benefits of \$42.8 million, beginning in fiscal year 2007. See also Note 17 beginning on page 107. Significant changes in expenditures also occurred in the following areas:

- *General Government* – Total expenditures in this category increased \$42.2 million. In addition to salary and benefit increases, additional funding was provided for the Governor's economic development plan, a new science and technology initiative (USTAR), and tourism marketing.
- *Human Services and Youth Corrections* – Total expenditures in this category jumped \$33 million due to increased funding and demand for substance abuse and mental health services, people with disabilities, and child and family services.
- *Higher Education* – Total expenditures in this category were up \$32.8 million, primarily due to salary increases, rate increases for retirement and health insurances, increased fuel and power costs, and increases in student financial aid.
- *Natural Resources* – Total expenditures in this category were up \$30.5 million, primarily due to an increase in capital budget expenditures in Parks and Recreation and Wildlife Resources.

Budgetary Highlights – General Fund

The Legislature adopted the initial fiscal year 2007 budget during the 2006 General Session. The original revenue estimates in the General Fund budget at the start of fiscal year 2007, excluding department-specific revenue sources such as federal grants, departmental collections, and including miscellaneous transfers, were 4.3 percent lower than the final fiscal year 2006 budget. The decrease was primarily due to the Legislature reducing the sales tax rate on unprepared food by 2 percent, effective January 1, 2007, and diverting additional sales tax revenue to fund highway projects. Budget expenditures were 7.4 percent higher than the final fiscal year 2006 budget. Carryover funds from fiscal year 2006 were used to fund this increase and offset the decrease in projected revenues. The Legislature increased funding for projected growth in Medicaid expenditures, capital development projects and building maintenance needs, and higher education. Other increases included funding for increases in employee salaries and benefits.

The budget was again addressed during the 2007 General Session of the Legislature (January to March 2007). General revenue estimates had increased \$211.7 million over those adopted in the 2006 General Session primarily due to increased revenue estimates for sales and use tax. Increased revenue estimates allowed the Legislature to designate \$223.6 million of expected excess revenue for fiscal year 2007 appropriations.

Final budgets of department-specific revenue sources increased over original budgets and actual department-specific revenues increased over final budgets mostly due to an increase in federal mineral lease revenues. Final budgets for many of the departmental-specific revenue sources and related expenditures such as federal grants, departmental collections, and miscellaneous revenues, are generally revised based on actual collections. The difference between final budgeted expenditures and actual expenditures is primarily due to nonlapsing and unspent restricted funds that will be carried forward to the next year. However, \$6 million of unspent budgeted dollars were lapsed back to the General Fund by agencies.

Education Fund

Effective July 1, 2006, the Legislature created the Education Fund and required that all taxes on income and the reserves of the Education Budget Reserve Account be accounted for in this new fund. As a result of this change, a reclassification of \$345.8 million was made to reduce beginning fund balance of the Uniform School Fund and increase the beginning fund balance of the Education Fund. The fund balance of the Education Fund (as adjusted) increased \$220.9 million or 63.9 percent because revenues exceeded transfers out of the fund. Education monies will be transferred out of the fund in the future for education needs.

Tax revenues now reported in the Education Fund increased \$297.2 million or 11 percent from the prior year as restated for comparability. Corporate taxes increased \$32.3 million or 8.5 percent and individual income taxes increased \$264.9 million or 11.4 percent. There are no expenditures reported in the Education Fund. However, \$2.787 billion was transferred out to fund public and higher education. The Uniform School Fund received \$2.190 billion, the General Fund received \$481.6 million, and the Nonmajor Governmental Funds received \$116 million for debt service and capital projects.

State law normally requires 25 percent of the "cumulative surplus" in the Education Fund and the Uniform School Fund to be transferred to the Education Budget Reserve Account. However, state law limits the combined totals of the General Fund Budget Reserve Account and the Education Budget Reserve Account to 6 percent of combined appropriations from certain funds. At yearend, the combined totals exceeded the 6 percent limit, and as a result, no surplus transfer was made. However, the Legislature appropriated \$13.4 million in fiscal year 2007 to the fund for use in any future budget shortfalls in education. Established by the Legislature in 2003, the Education Budget Reserve Account ended the year with a balance of \$142.8 million.

Uniform School Fund

As noted above, the beginning balance of the Uniform School Fund was reduced by \$345.8 million and the Education Fund beginning balance was increased by the same amount as a result of the reclassification of fund balance. After this adjustment, the fund balance in the Uniform School Fund increased \$55.1 million or 9.2 percent from the prior year, due in part to an \$8.4 million increase in revenues from excess unclaimed property and a \$7.3 million increase in investment income. The remaining increase in fund balance was the result of additional transfers from the Education Fund to support future public education expenditures. Expenditures for public education increased by \$224.3 million or 9.7 percent, as the Legislature increased the budget for enrollment growth and for increased costs related to employee salary and benefit increases. The Uniform School Fund ended the year with a "surplus" from unreserved and undesignated sources of \$176.9 million.

Transportation Fund

The fund balance of the Transportation Fund increased \$117.1 million or 55.8 percent from the prior year. The increase was primarily due to additional net transfers (appropriations) into the fund for highway projects, much of which were unspent at June 30, 2007. In addition, revenues increased by \$34 million or 4 percent, largely due to a \$21.5 million increase in the motor and special fuels tax and a \$6.6 million increase in federal aeronautics revenue. Also, expenditures increased by \$57.4 million or 7.2 percent as a result of increased spending on federal participating highway projects.

Authorized federal funding for highway construction remains relatively stable from year to year. However, the spending of state and federal revenue reflects the timing of highway construction projects, which is impacted by a variety of circumstances such as environmental studies or weather. Also, the Department of Transportation has discretion on allocating federal funds among projects, which impacts the amount of federal revenue reported in the Transportation Fund and Transportation Investment Fund.

Transportation Investment Fund

The fund balance of the Transportation Investment Fund decreased by \$14.4 million or 10 percent from the prior year. Revenues in the fund increased \$173.3 million or 181.4 percent, mostly due to an increase in sales and use taxes of \$154.3 million as a result of House Bill 112, *Transportation Investment Act*, of the 2006 General Session. This bill codified that 8.3 percent of general sales tax revenue be used for Centennial Highway projects accounted for within this fund. Federal contracts and grants revenues also increased \$18.6 million or 343.6 percent due to the receipt of federal funds for the previously completed I-15 reconstruction project. Expenditures in the fund increased by \$187.7 million or 106.5 percent primarily in construction expenditures for the projects specific to this fund.

Trust Lands Fund

The fund balance of the permanent Trust Lands Fund increased by \$232.9 million or 31 percent due to revenues generated from land use, sales of trust lands, and investment income. The permanent fund also generated \$25.6 million of cash investment earnings for the Uniform School Fund that is earmarked for distribution to local school districts. The principal in the fund is held in perpetuity with earnings restricted primarily to support public education.

FINANCIAL ANALYSIS OF THE STATE'S PROPRIETARY FUNDS**Student Assistance Programs**

The Student Assistance Programs finished the year with an increase in net assets of \$22.6 million or 8.5 percent. The increase was largely due to an increase in investment income. Federal reinsurance reimbursements decreased \$9.1 million or 21.3 percent due to a decrease in the number of claims paid by lenders on defaulted loans. Of total net assets of \$287.7 million, \$195.9 million is restricted for use within the Student Assistance Programs by bond covenants or by federal law.

Unemployment Compensation Fund

The State's unemployment rate decreased slightly compared to the rate one year ago. The improving employment situation resulted in a \$4.8 million or 4.7 percent decrease in benefit payments from the prior year. For the third consecutive year, employer taxes and other revenues exceeded benefit payments. Assets were sufficient to handle the demand for benefits, and net assets increased \$150.9 million or 22 percent, to \$838.1 million. The entire balance of net assets in this fund is restricted for paying unemployment benefits by state and federal law.

Water Loan Programs

The net assets of the Water Loan Programs increased \$44.7 million or 7.5 percent from the prior year. Additional capital for loans was provided from \$24.9 million in dedicated sales tax revenues and \$18.3 million in federal grants, in addition to net operating revenues in the fund. Of total net assets of \$642.7 million, \$259.2 million is restricted for use within the Water Loan Programs by federal grant requirements. In addition, loans receivable for the programs increased \$19.8 million or 4 percent over the prior year.

CAPITAL ASSET AND LONG-TERM DEBT ADMINISTRATION

Capital Assets

The State's capital assets increased a net \$617.1 million during the year. The change consisted of net increases in infrastructure (e.g., highways) of \$155.4 million; land and related assets of \$36.3 million; and buildings, improvements, and construction in progress of \$421.1 million. Machinery and equipment increased a net \$4.3 million during the year. Many buildings financed by the State are actually owned by the colleges and universities, which are discrete component units of the State. Therefore, while the capital assets are on the component unit's financial statements, any outstanding debt issued by the State to finance construction of those assets is reported as a liability of the State's governmental activities. This in turn reduces unrestricted net assets. As of June 30, 2007, the State had \$28.5 million of outstanding debt related to capital assets of component units.

At June 30, 2007, the State had \$243.3 million in commitments for building projects in its capital projects funds, and \$593.7 million (\$242.9 million in the Transportation Investment Fund and \$350.8 million in the Transportation Fund) in commitments for highway construction and improvement projects. Funding for the commitments will come from existing resources in these funds and from future bond proceeds and appropriations.

The State has adopted an allowable alternative to reporting depreciation for roads and bridges (infrastructure assets) maintained by the Utah Department of Transportation (UDOT). Under this alternative method, referred to as the "modified approach," UDOT must maintain an asset management system and demonstrate that the infrastructure is being preserved at or above established condition levels. Infrastructure assets accounted for under the modified approach are not depreciated, and maintenance and preservation costs are expensed.

The State's established condition level for roads is to maintain 50 percent with a rating of "fair" or better and no more than 15 percent with a "very poor" rating. The most recent condition assessment, completed for calendar year 2006, indicated that 64.5 percent of the roads were in "fair" or better condition. Only 11.3 percent of the roads assessed were in "very poor" condition. These results reflect a slight decline from conditions in calendar year 2005, when 69.5 percent of the roads were assessed as "fair" or better, and 6.3 percent assessed were in "very poor" condition.

The State's established condition level for bridges is to maintain 50 percent with a rating of "good" and no more than 15 percent of bridges with a "poor" rating. The most recent condition assessment, completed in April 2007, indicated that 71 percent and 2 percent of bridges were in "good" and "poor" condition, respectively. These results are similar to the prior year.

During fiscal year 2007, the State spent \$459.2 million to maintain and preserve roads and bridges. This amount is 21.3 percent above the estimated amount of \$378.6 million needed to maintain these assets at established condition levels.

More information about capital assets is included in Note 8 on page 84, and more detailed information on the State's modified approach for reporting infrastructure is presented in the Required Supplementary Information on page 120.

Long-term Debt

The *Constitution of Utah* authorizes general obligation borrowing only as approved by the Legislature. The *Constitution* also limits outstanding state general obligation debt to 1.5 percent of the fair market value of all taxable property in the State, while state law further restricts outstanding state general obligation debt to no more than 45 percent of the appropriations limit. As of June 30, 2007, the State was \$531.1 million below the statutory debt limit and \$2.211 billion below the debt limit established in the *Constitution*. Revenue bonds are not backed by the general taxing authority of the State, but are payable solely from specific fees or loan repayments as pledged in the bond indentures.

State of Utah
Net Outstanding Bonded Debt as of June 30
(Expressed in Millions)

	Governmental Activities		Business-type Activities		Total Primary Government		Total Percentage Change
	2007	2006	2007	2006	2007	2006	2006 to 2007
General Obligation Bonds	\$ 1,284.0	\$ 1,436.8	\$ —	\$ —	\$ 1,284.0	\$ 1,436.8	(10.6)%
Revenue Bonds:							
State Building Ownership Auth.	275.5	295.6	37.0	38.3	312.5	333.9	(6.4)
Student Assistance Programs	—	—	2,137.7	2,138.1	2,137.7	2,138.1	(0.0)
Total Bonds Payable	\$ 1,559.5	\$ 1,732.4	\$ 2,174.7	\$ 2,176.4	\$ 3,734.2	\$ 3,908.8	(4.5)%

The State issued no new general obligation bonds or revenue bonds during fiscal year 2007.

The State's active management of its resources has helped the State maintain its triple-A rating on general obligation bonds from all three national rating agencies, and double-A rating on lease revenue bonds from two national rating agencies from which ratings were sought. These ratings are the best available and save millions of dollars in interest each year because the State is able to obtain very favorable interest rates on new debt. Note 10 beginning on page 88 contains more information about the State's outstanding debt.

ECONOMIC OUTLOOK AND NEXT YEAR'S BUDGET

Tax revenues are expected to increase moderately in fiscal year 2008. However, original general revenue estimates for the General Fund, Education Fund and Uniform School Fund for fiscal year 2008 are slightly lower than actual fiscal year 2007 revenues. This is because actual fiscal year 2007 revenues were stronger than anticipated, creating a surplus. The Legislature balanced the 2008 budget primarily by using anticipated 2007 carryover funds of \$787.3 million and utilizing other miscellaneous sources. The Legislature appropriated substantial amounts of new and ongoing money to public and higher education. Other areas that received increased funding were roads and highways, capital projects, Medicaid, and substance abuse prevention and treatment. The Legislature also appropriated \$40 million to the Education Budget Reserve Account to cover any future budget shortfalls in education. State employees were provided a 3.5 percent cost-of-living adjustment. An additional 1.5 percent in discretionary monies was funded to alleviate department-specific compensation problems. Other postemployment benefits were funded with approximately \$54 million.

Revenue collections to date in fiscal year 2008 are in line with original estimates. Utah's economy is expected to remain stable in the near future. The average unemployment rate is expected to decline in 2007 to 2.7 percent, down from the average 2006 rate of 2.9 percent. Taxable retail sales are expected to increase 7.3 percent by the end of 2007 and growth in personal income is expected to be 9 percent for the same period. Because these indicators are measured on a calendar-year basis, the impact on the State budget will not be fully realized until well into fiscal year 2008.

CONTACTING THE STATE'S DIVISION OF FINANCE

This financial report is designed to provide our citizens, taxpayers, customers, investors, and creditors with a general overview of the State's finances and to demonstrate the State's accountability for the money it receives. If you have questions about this report or need additional financial information, please contact the Department of Administrative Services: Division of Finance, Financial Reporting Section at (801) 538-3082 or visit our Web site at: www.finance.utah.gov.

The preceding discussion and analysis focuses on the State's primary government operations. With the exception of a few nonmajor component units, the State's component units each issue separate audited financial statements that include their respective management's discussion and analysis. Component unit statements may be obtained from their respective administrative offices or from the Utah State Auditor's Office, Utah State Capitol Complex, East Office Building, Suite E310, Salt Lake City, UT 84114.

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